

DEPARTMENT OF ECONOMIC DEVELOPMENT
STATE OF LOUISIANA



PROCEDURAL REPORT
ISSUED AUGUST 2, 2006

**LEGISLATIVE AUDITOR
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In compliance with the Americans With Disabilities Act, if you need special assistance relative to this document, or any documents of the Legislative Auditor, please contact Wayne "Skip" Irwin, Director of Administration, at 225/339-3800.



STEVE J. THERIOT, CPA
LEGISLATIVE AUDITOR

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June 23, 2006

DEPARTMENT OF ECONOMIC DEVELOPMENT
STATE OF LOUISIANA
Baton Rouge, Louisiana

As required by Louisiana Revised Statute 24:513, we conducted certain procedures at the Department of Economic Development for the period from July 1, 2004, through June 23, 2006. Our procedures included (1) a review of the department's internal controls; (2) tests of financial transactions; (3) tests of adherence to applicable laws, regulations, policies, and procedures governing financial activities; and (4) a review of compliance with prior year report recommendations. Our procedures were more limited than would be necessary to give an opinion on internal control and on compliance with laws, regulations, policies, and procedures governing financial activities.

Specifically, we interviewed management personnel and selected departmental personnel and evaluated selected documents, files, reports, systems, procedures, and policies, as we considered necessary. After analyzing the data, we developed recommendations for improvement. We then discussed our findings and recommendations with appropriate management personnel before submitting this written report.

The Annual Fiscal Report of the Department of Economic Development was not audited or reviewed by us, and, accordingly, we do not express an opinion on that report. The department's accounts are an integral part of the State of Louisiana's financial statements, upon which the Louisiana Legislative Auditor expresses opinions.

In our prior report on the Department of Economic Development, dated May 6, 2004, we reported findings relating to noncompliance with certain federal and state requirements of the Temporary Assistance for Needy Families Program, insufficient monitoring of contract payments, and leave use not required and work hours uncertified. These findings have been resolved by management.

Based on the application of the procedures referred to previously, all significant findings are included in this report for management's consideration.

**No Independent Review of Expenses
Reported for Movie Tax Credits**

The Department of Economic Development (LED) issued investor and labor tax credits totaling \$191.8 million from 2002 to 2005 without obtaining an independent review validating the motion picture production companies' expenses that were used by the

production companies to calculate their tax credits. Good internal control requires independent verification of expenses before state credits are issued. Effective January 1, 2006, Act 456 of the 2005 Regular Legislative Session now requires motion picture production companies to submit a cost report of production expenditures that is audited and certified by an independent certified public accountant. However, no independent audit requirement existed before that time.

Production companies submit cost reports of production expenses to LED. A cost report is prepared by the production company's accounting department and the tax credits are calculated by the company from the cost report, which is certified by the production company's legal counsel. The production company's legal counsel then submits the production costs and tax credits to LED. LED then issues the company a tax credit certification letter.

From 2002 to 2005, there were \$171,365,623 in investor tax credits and \$20,425,979 in labor tax credits that were issued to motion picture production companies in Louisiana. No independent reviews were required or performed by LED on expenses used in determining these tax credits. LED relied upon the affidavit submitted by the production company's legal counsel to attest to the amount of expenses made and credits earned. As a result, LED relied on the production company to tell the state how much the credit should be without independent verification and the state had no certainty as to the correctness of the amounts.

LED management should consider going back and verifying production company expenses for previously issued credits. LED should ensure that audits are obtained on all production company expenditures for credits occurring after January 1, 2006. Management did not concur with the finding noting that the production cost reports and supporting documentation were reviewed to verify actual investment and expenditures made by the production companies (see Appendix A, pages 1-2).

Additional Comments: In our testing, we asked to see all documentation reviewed by the department before the tax credits were granted. The information provided to us for our test sample did not include the detailed items such as bank check registers, receipts, and paid invoices mentioned in management's response. In addition, audit procedures disclosed no evidence of a detailed review. Detailed documentation of production cost is maintained by production company personnel and not by the department.

Noncompliance With Enterprise Zone Program Regulation

LED did not comply with the Enterprise Zone Program regulation regarding Inspection/Audit Affidavits. Louisiana Administrative Code Title 13 Part 1 Chapter 7 Section 725(D) states that the applicant shall file an original and a copy of the Inspection/Audit Affidavit Form showing a complete list of buildings and equipment and the cost of each item on the project with the appropriate fee for the inspection, which will be completed by the Business Incentives Division of the Office of Business

Development. This affidavit must be filed within six months of the project/construction ending date or when the signed original contracts are returned to the Business Incentives Division, whichever is later.

In a review of 12 contracts, 10 (83%) contracts did not have the Inspection/Audit Affidavit filed within the required time frame. As of March 28, 2006, five Inspection/Audit Affidavit forms have yet to be submitted and are between 4 to 14 months overdue while five forms were submitted between 3 to 7 months late. In addition, since a \$100 fee must be submitted with an inspection/audit affidavit form, LED is not collecting this fee in a timely manner.

LED has not placed sufficient emphasis on ensuring that an Inspection/Audit Affidavit was performed and filed timely as required. Failure to obtain an Inspection/Audit Affidavit for each business receiving Enterprise Zone tax credits increases the risk that tax credits may have been granted based on inaccurate or incomplete data and places the department in noncompliance with program regulations.

LED management should ensure that Audit/Inspection Affidavits are submitted in compliance with Enterprise Zone Program regulations and that fees are collected timely. Management concurred with the finding and provided a corrective action plan (see Appendix A, pages 3-4).

Lack of a Current Disaster Recovery/Business Continuity Plan

LED does not have a current disaster recovery/business continuity plan. The Office of Information Technology Policy Number 11 requires state entities to develop, test, and maintain disaster recovery and business continuity plans designed to ensure the availability of mission-critical services and functions in the event of a disaster or unscheduled event that would impact the agency's information technology (IT) and telecommunications systems.

LED contracted with a vendor to update its 1996 disaster recovery/business continuity plan. A new plan was to be drafted in 2004, but it was never completed. No further progress has been made on the plan since 2004. Failure to maintain a current disaster recovery/business continuity plan increases the risk that untimely or excessive delays in processing critical data may occur and that critical data may be lost.

LED management should prepare a current written disaster recovery/business continuity plan that is tested periodically and updated as necessary to ensure that the plan continues to meet the department's needs. Management partially concurred with the finding, but plans to have a contract in place by June 1, 2006, which upon completion will result in a current disaster recovery/business continuity plan (see Appendix A, page 5).

Lack of Controls Over Certificates of Deposit

LED lacks proper controls over monitoring and accounting for the certificates of deposit (CDs) pledged for Small and Emerging Business Development Program projects. CDs are pledged as collateral against letters of credit issued by the state for Small and Emerging Business Development Program projects. An irrevocable letter of credit (bond guarantee) is issued by the state as collateral on the bonds that are issued for the Small and Emerging Business Development Program projects. Good internal control requires that records be maintained to ensure that all transactions that affect both the accounting records and bank accounts are in agreement and that no errors or fraud has occurred. In addition, good internal control requires establishing formal written procedures for accurately compiling financial information included in the department's Annual Fiscal Report (AFR).

Audit procedures were performed on all 10 outstanding CDs that were recorded in LED's 2005 AFR and disclosed the following deficiencies:

- LED does not properly monitor CD activity relating to the Small and Emerging Business Development Program. LED was not aware that two CDs with maturity dates of September 24, 2004, and January 21, 2005, totaling \$101,545 had matured with the money being sent to the surety company instead of LED. In addition, as of June 30, 2005, interest totaling nearly \$6,000 on six CDs was rolled over into renewed CDs instead of being sent to LED.
- LED could only provide supporting documentation (Certificate of Deposit Receipt and/or the Maturity and Automatic Renewal Notice) for five of the 10 CDs.
- The 2005 AFR note disclosure regarding CD balances was overstated by \$297,239. Documentation maintained for reporting purposes was inaccurate as information was not properly updated or supported.

LED does not properly monitor the activity of the CDs pledged for Small and Emerging Business Development Program projects and does not maintain the proper documentation to support CD amounts. Failure to monitor the CD activity and maintain adequate documentation increases the risk that errors and/or fraud may occur and not be detected in a timely manner.

LED management should ensure that CDs pledged for Small and Emerging Business Development Program projects are properly monitored and accurately accounted for in the department's AFR. Management partially concurred with the finding noting that LED does have controls over the monitoring of CDs pledged for the projects. Management also noted that steps have been taken to ensure that all documentation is on file and that LED is working with each party involved in the Small and Emerging Business Development Program to ensure that procedures are followed (see Appendix A, pages 6-7).

Additional Comments: If proper monitoring procedures were in place, LED would have maintained supporting documentation of each CD transaction; would have realized that interest on CDs was being rolled over instead of being sent to LED; and would have known the status of each CD. However, information had to be obtained from the banks and sureties regarding the current status of several CDs.

**No Comprehensive Risk-Based
Internal Audit Plan**

LED does not have a comprehensive risk-based internal audit plan to serve management in examining, evaluating, and reporting on its internal control, including information technology, and evaluating its compliance with the policies and procedures of the control system. The department's internal audit charter indicates that the professional standards outlined in the Statements on Internal Auditing Standards will be followed. The standards require that the internal audit plan of engagements should be based on a risk assessment, undertaken at least annually. In addition, LED's internal audit charter provides that one of the internal auditor's responsibilities is to develop an annual audit plan using an appropriate risk-based methodology, including any risks or control concerns identified by management with the objectives of continually assessing all high-risk areas of LED and evaluating critical business processes throughout LED.

A review of the LED internal audit function disclosed that no comprehensive risk-based audit plan was developed for fiscal year 2005 or fiscal year 2006. Failure to develop a comprehensive risk-based audit plan that properly guides audit scheduling hinders the effectiveness of the internal audit function. In addition, the lack of a comprehensive risk-based audit plan is in noncompliance with LED's internal audit charter.

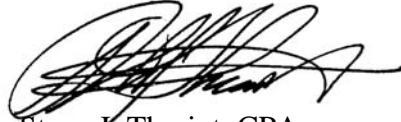
LED management should improve the effectiveness of its internal audit function by ensuring that a comprehensive risk-based audit plan is prepared annually. Management partially concurred with the finding and noted that the process to determine the fiscal year 2007 risk-based audit plan will be documented (see Appendix A, pages 8-9).

The recommendations in this report represent, in our judgment, those most likely to bring about beneficial improvements to the operations of the department. The varying nature of the recommendations, their implementation costs, and their potential impact on the operations of the department should be considered in reaching decisions on courses of action. Findings relating to the department's compliance with applicable laws and regulations should be addressed immediately by management.

DEPARTMENT OF ECONOMIC DEVELOPMENT

This report is intended solely for the information and use of the department and its management and is not intended to be, and should not be, used by anyone other than these specified parties. Under Louisiana Revised Statute 24:513, this report is distributed by the Legislative Auditor as a public document.

Respectfully submitted,

A handwritten signature in black ink, appearing to read 'Steve J. Theriot', written over a horizontal line.

Steve J. Theriot, CPA
Legislative Auditor

NWM:EFS:PEP:ss

[DED06]

Management's Corrective Action
Plans and Responses to the
Findings and Recommendations



State of Louisiana

LOUISIANA ECONOMIC DEVELOPMENT

Kathleen Babineaux Blanco
Governor

Michael J. Olivier
Secretary

May 18, 2006

Mr. Steve J. Theriot, CPA
Legislative Auditor
1600 North Third Street
Baton Rouge, LA 70804-9397

Dear Mr. Theriot:

This is in response to your request to provide your office an official response relating to the audit finding regarding No Independent Review of Expenses Reported for Movie Tax Credits.

Louisiana Economic Development (LED) does not concur with the finding concerning no independent review of expenses for movie tax credits. Prior to the enactment of ACT 456 of the Regular Session 2005, the Governor's Office of Film and Television Development (GOFTD) reviewed "entertainment industry standard" production costs reports and the cost reports' accompanying documentation (i.e., bank check registers, receipts, paid invoices, wage reports and/or other relevant supporting documentation) to verify the actual investment and expenditure made by the state-certified production company. The practice by the agency was in full compliance with the law that required only the submission of a cost report of production expenditures. During this time frame, no funding was made available to LED or the Program, nor was any recommendation made by the Legislative Auditor to provide the professional audit that is now recommended. The productions' cost reports and the relevant supporting documentation were certified by GOFTD, not the legal counsel of the production company. The incentive program also required that all expenditures must be made from a Louisiana checking account. In fact, the film could not be made and distributed into commerce unless the actual investment and expenditures were made according to produced "entertainment industry standard" production cost reports, which the GOFTD reviewed throughout the duration of the production.

Wages paid to Louisiana residents were also 3rd party validated by the local trade union which was the primary provider of the Louisiana-based below-the-line crew for the productions claiming the labor credit (Louisiana Employment Tax Credit). The GOFTD always performed the necessary review to ensure the accuracy of the production cost reports as provided by the production company.

May 18, 2006

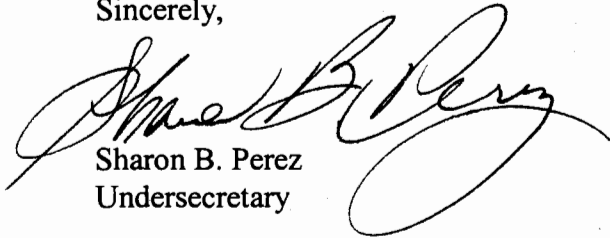
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It also should be noted that it is not in the best interest of these licensed and bonded film production companies and, in some cases, publicly traded companies to submit inaccurate information to claim a tax credit for transfer to a Louisiana resident that will be claimed on a state tax return submitted to the Department of Revenue and subject to further review.

In 2005, LED along with the GOFTD proactively initiated legislation to strengthen our oversight of the program. With the passage of ACT 456, the GOFTD now requires an independent audit of the expenditure cost report, conducted by a Louisiana Licensed Certified Public Accountant, to be submitted to GOFTD before we certify any credits. The Department contracted with an outside auditor to provide appropriate guidance in implementing the audit requirement. This demonstrates an evolutionary step in the program that will continue to maintain adequate internal controls. This practice went into effect before January 1, 2006 and continues to be followed.

If you require further assistance, please contract me at 225/342-5361.

Sincerely,



Sharon B. Perez
Undersecretary

SBP:WB:cs

cc: Nicole W. Martin, CPA
Senior Auditor

Ernest F. Summerville, Jr., CPA
Audit Manager



State of Louisiana

LOUISIANA ECONOMIC DEVELOPMENT

Kathleen Babineaux Blanco
Governor

Michael J. Olivier
Secretary

June 1, 2006

Mr. Steve J. Theriot, CPA
Legislative Auditor
1600 North Third Street
Baton Rouge, LA 70804-9397

Dear Mr. Theriot:

This is in response to your request to provide your office an official response relating to the audit finding regarding Enterprise Zone Program Regulation.

Louisiana Economic Development concurs with the finding. The finding states that 10 out of 12 contracts reviewed did not have the inspection/audit affidavit on file within the prescribed time frame.

Inspections have not been performed after the completion of projects as frequently as possible due to lack of personnel. Another problem is lack of tracking capabilities in the data base we currently use.

We have taken the following steps and have placed them in operation:

- An affidavit will be sent when the approved contract is mailed to the contractor for their signature.
- Staff will emphasize the inspection/audit affidavit provision in the future workshops they conduct.
- For the affidavits that are not on file presently, we will request them to be submitted as soon as possible along with the appropriate fee.

LED has taken steps to ensure that the inspection affidavits are received when required and will strive to perform more site inspections as personnel become available to perform this function.

If you require further assistance, please contract me at 225/342-5361.

Sincerely,

A handwritten signature in black ink, reading "Sharon B. Perez". The signature is written in a cursive, flowing style with a large initial 'S' and a long, sweeping underline.

Sharon B. Perez
Undersecretary

SBP:WB:cs

cc: Nicole W. Martin, CPA
Senior Auditor

Ernest F. Summerville, Jr., CPA
Audit Manager



State of Louisiana

LOUISIANA ECONOMIC DEVELOPMENT

Katrinee Sabineaux Blanco

Governor

May 8, 2006

Michael J. Olivier

Secretary

Mr. Steve J. Theriot, CPA
Legislative Auditor
1600 North Third Street
Baton Rouge, LA 70804-9397

Dear Mr. Theriot:

This is in response to your request to provide your office an official response relating to the audit finding regarding Lack of Current Disaster Recovery/Business Continuity Plan.

The department partially concurs with this finding. The current disaster recovery/business continuity plan is not up to date with the latest names and phone numbers of the department's employees. However, the department does have a process in place to contact its current employees if a disaster or some other event occurs that prevents the use of our building. Our fiscal and payroll accounting functions are processed by Integrated Statewide Information Systems (ISIS) which is housed in another building.

We have begun to obtain information to have an outside contractor write a current business continuity plan with the current names and addresses of all of our employees along with a written disaster recovery plan. The contract should be in place by June 1, 2006 with a basic written document prepared within 60 days after then. This should put us in compliance with the requirements of the Governor's Office of Homeland Security and Emergency Preparedness. This plan will be tested and updated as necessary to meet the department's needs and objectives.

If you require further assistance, please contact me at 225/342-5361.

Sincerely,

A large, stylized handwritten signature in black ink, appearing to read "Sharon B. Perez".

Sharon B. Perez
Undersecretary
SBP:WB:cs

cc: Nicole W. Martin, CPA
Senior Auditor

Ernest F. Summerville, Jr., CPA
Audit Manager

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AN EQUAL OPPORTUNITY EMPLOYER



State of Louisiana

LOUISIANA ECONOMIC DEVELOPMENT

Kathleen Babineaux Blanco
Governor

Michael J. Olivier
Secretary

May 18, 2006

Mr. Steve J. Theriot, CPA
Legislative Auditor
1600 North Third Street
Baton Rouge, LA 70804-9397

Dear Mr. Theriot:

This is in response to your request to provide your office an official response relating to the audit finding regarding Monitoring of Certificates of Deposits for the Small and Emerging Business Development Program.

We partially concur with the finding concerning the monitoring of the certificates of deposits for the Small and Emerging Business Development program. Louisiana Economic Development (LED) does have controls over the monitoring of Certificates of Deposit (CD) pledged for the Small and Emerging Business Development Bonding Assistance Program. Projects are routinely monitored to determine if and when CDs are returned to the Department.

Due to turnover at the bank and lack of communication among sections of the bank, LED did not receive paper documentation from the bank in accordance with established procedures. In addition, the bank did not rollover two projects causing the surety to surrender the applicable Irrevocable Line of Credit in order to ensure collateral until projects are completed in accordance with the Bonding Assistance Program agreement. LED had full knowledge of these situations and understood that funds would be returned upon completion of projects. The entire \$101,545 has been returned to LED, as projects have been completed and LED has been able to account for all funds used as collateral.

We have been monitoring this program and have taken steps to assure that all the documentation is on file and the bank, contractor, surety, and LED are working together to ensure that the procedures are followed. LED has met with bank personnel to discuss the processes of the surety collateral program and ways to improve it.

We agree that documentation was not in the file for five of the certificates of deposit at the time of the audit but are in the file now.

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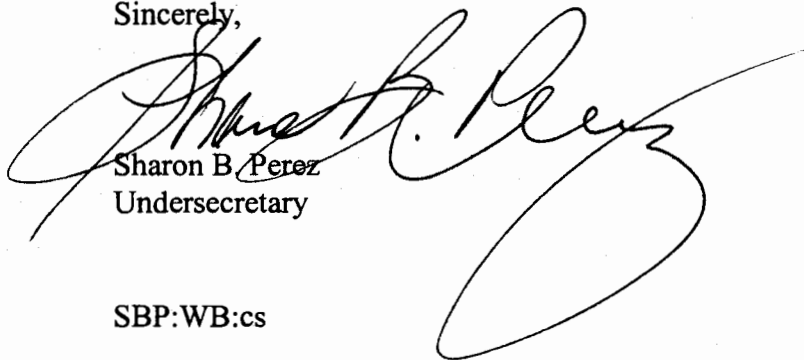
May 18, 2006

Page 2

While the note disclosure for this program in the annual financial report was overstated, the Office of Statewide Reporting and Accounting Policy was notified of the correct amounts to include in the report.

If you require further assistance, please contact me at 225/342-5361.

Sincerely,

A large, stylized handwritten signature in black ink, appearing to read 'Sharon B. Perez', is written over the typed name and title.

Sharon B. Perez
Undersecretary

SBP:WB:cs

cc: Nicole W. Martin, CPA
Senior Auditor

Ernest F. Summerville, Jr., CPA
Audit Manager



State of Louisiana

LOUISIANA ECONOMIC DEVELOPMENT

Kathleen Babineaux Blanco
Governor

Michael J. Olivier
Secretary

May 8, 2006

Mr. Steve J. Theriot, CPA
Legislative Auditor
1600 North Third Street
Baton Rouge, LA 70804-9397

Dear Mr. Theriot:

This is in response to your request to provide your office an official response relating to the audit finding regarding No Comprehensive Risk-Based Internal Audit Plan.

We partially concur with this finding that states the Department of Economic Development (LED) does not have a comprehensive risk-based internal audit plan. The internal audit plans for fiscal year 2005 and 2006 were developed with management's assistance based on activities in the department considered to add value and improve our operations. While the audit plan was not supported by written documentation that described the risk-based functions that internal audit should audit, the audit plan was based on decisions by management and the auditor to evaluate the adequacy of controls and functions to meet management's objectives.

Another reason for the partial concurrence is that the Department in 2005 obtained its International Organization for Standardization ISO Certification and is the only state economic development agency in the United States that is ISO certified. Organizations such as LED pursue ISO certification to demonstrate commitment to quality procedures, safety, environmental responsibility and customer service and must meet stringent requirements set by ISO, a network of the national standards institutes of 151 countries.

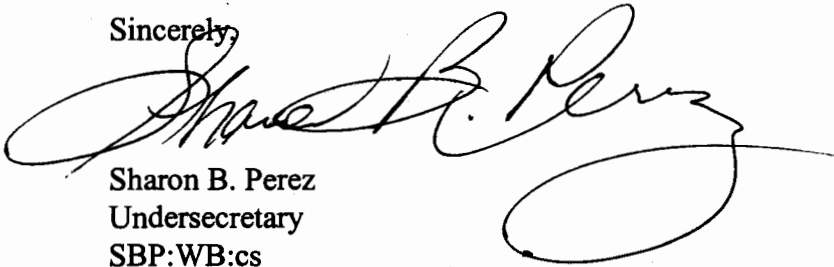
In order to become certified, LED had to maintain a system for improving service delivery to customers through quality management practices. LED was re-certified in 2006.

Page 2
May 8, 2006

The internal auditor is currently in the process of obtaining input from all areas of the department to make an assessment of the risk of achieving the department's objectives. The audit plan for the 2006 – 2007 fiscal year will be risk-based determined by a documented process to which management and internal audit has agreed. This plan should be completed by the end of May, 2006.

If you require further assistance, please contract me at 225/342-5361.

Sincerely,

A handwritten signature in black ink, appearing to read "Sharon B. Perez", with a large, stylized loop at the end.

Sharon B. Perez
Undersecretary
SBP:WB:cs

cc: Nicole W. Martin, CPA
Senior Auditor

Ernest F. Summerville, Jr., CPA
Audit Manager